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No.

The Supreme Court of the United States

OCTOBER TERM, 1981

STEPHEN L. BEST, LETTY SHEILD BEST, EDWARD E. FIRTH, AND ANNA WESTWOOD FIRTH,
Petitioners,

v.

UNITED VIRGINIA BANK/NATIONAL AND UNITED VIRGINIA MORTGAGE CORPORATION,
Respondents.

ON APPEAL FROM THE SUPREME COURT OF VIRGINIA

PETITION FOR WRIT OF CERTIORARI

GRAYSON P. HANES
HAZEL, BECKHORN AND HANES
P. O. Box 547
4084 University Drive
Fairfax, Virginia 22030
(703) 273-6644
Counsel for Petitioners and Counsel of Record

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TO: THE HONORABLE CHIEF JUSTICE AND ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES

Stephen L. Best, Letty Sheild Best, Edward E. Firth, and Anna Westwood Firth, the Petitioners herein pray that a Writ of Certiorari issue to review the judgment of the Supreme Court of Virginia in the above case dated January 22, 1982, with rehearing denied on March 12, 1982.

QUESTION PRESENTED FOR REVIEW

Did the Supreme Court of Virginia violate the provisions of the Fourteenth Amendment of the United States Constitution when it held that a lender can, by agreement with a borrower, possess the unrestricted right to forbid transfer of title to property securing a debt of such lender?

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OPINION BELOW

The opinion of the Supreme Court of Virginia is reported as follows: *United Virginia Bank/National, et al.*, v. *Stephen L. Best, et al.*, 223, Va. ....., 286 S.E.2d 221 (1982). This opinion is printed in the Appendix, *infra* at page A-1

The order denying the petition for rehearing is printed in the Appendix, *infra*, at page A-5.

JURISDICTION

The decision of the Supreme Court of Virginia in *Best* was dated January 22, 1982. A timely notice and petition for rehearing were filed, and pursuant to Rule 5:53(a) of the Rules of the Supreme Court of Virginia, the clerk of that Court withheld certification of the mandate of the opinion until the petition for rehearing was disposed of. The petition for rehearing was denied on March 12, 1982.

The jurisdiction of this Court is invoked pursuant to Title 28, UNITED STATES CODE, Section 1257 (3):

> By writ of certiorari, . . . where any title, right, privilege, or immunity is specially set up or claimed under the Constitution . . . of . . . the United States.

The specific provision of the Constitution which is violated is the 14th amendment which provides:

> . . . no state shall make or enforce any law which shall abridge the privileges . . . of citizens of the United States; nor shall any state deprive any person of . . . property, without due process of law. . . .

In the present case the Bests (Purchasers) purchased property from the Firths (Borrowers) assuming a note se-

cured by a deed of trust in favor of United Virginia Bank/ National (Lender). The deed of trust provided in part:

> . . . and the said parties of the first part [Borrowers], in order more fully to protect the security of this deed of trust, do hereby agree as follows:
>
> . . . 7. The maker of the note covenants and agrees that he will not assign or transfer the property secured by this deed of trust without prior approval of the noteholder.

The Lender refused to allow the Purchasers to take title to the property and assume the deed of trust unless they agreed to increase the interest rate and pay one point. The Purchasers claimed that this was an unreasonable restraint on alienation of title, and brought suit for declaratory judgment in the Circuit Court of Fairfax County. The Circuit Court of Fairfax County found that transfer of title to the Purchasers did not impair the security of the Lender, which was a requirement under the deed of trust and ruled that the terms and conditions imposed by the Lender represented an unreasonable restraint on alienation of title. The decree of the Circuit Court is printed in the Appendix, *infra*, at page A-6.

The Lender appealed to the Supreme Court of Virginia on the principle that there was no restraint on alienation, and if there were, that the restraint was not unreasonable. Having prevailed in the lower court, the Borrowers and Purchasers defended on the basis of the lower court ruling that the Lender had not shown an impairment of security as required by the deed of trust.

In its decision the Supreme Court of Virginia decided the case on a legal principle which had never been raised

in the proceedings before the Circuit Court or the Supreme Court of Virginia, that is, that the prefatory or recital language in the deed of trust conflicted with the obligatory provision of covenant 7, and, therefore, the obligatory provision prevailed. The Court also misapplied that principle of law, as is shown later in the Petitioners' argument.

The Court did not consider whether the consent requirement of Covenant 7 constituted an unreasonable restraint on alienation.

The only conclusion that can be drawn from the decision of the Supreme Court of Virginia is that a lender has the right to forbid the conveyance of property by its borrower without restriction. This position was not advanced by the Lender, and it came as a complete suprise to the Petitioners. The decision is totally repugnant to the Fourteenth Amendment of the United States Constitution.

The Petitioners filed a petition for rehearing, pointing out that the legal principle upon which the Court decided the case had not been advanced by the Lender, that the principle was misapplied, and that reliance upon the principle would result in an unlimited and unrestricted restraint on alienation, which would be contrary to the Fourteenth Amendment of the Constitution. Essential parts of the petition for rehearing are printed in the Appendix, *infra*, at page A-10.

The petition for rehearing was summarily denied.

The Supreme Court has jurisdiction to grant certiorari as the decision was a total surprise, and could not have been anticipated on the basis of prior rulings and the principle advanced by the Lender. *Herndon* v. *Georgia*, 295, U.S. 441, 55 S.Ct. 794 (1935). The reasons why such decision could not have been anticipated are set forth in greater detail in the Petitioners' argument.

STATEMENT OF THE CASE

In August, 1972, Edward and Anna Firth (Borrowers) acquired property in Fairfax County, Virginia. In order to obtain the purchase money, they executed a promissory note, dated September 25, 1972, payable to United Virginia Bank/National (Lender), for $66,800.00, with interest at the rate of 7½% per annum. This note was secured by a deed of trust containing the following language:

> . . . and the said parties of the first part [Borrowers], in order more fully to protect the security of this deed of trust, do hereby agree as follows:
>
> . . . 7. The maker of the note covenants and agrees that he will not assign or transfer the property secured by this deed of trust without prior approval of the note holder.

The deed of trust further provided that if any covenant was violated by the Borrowers, the indebtedness would immediately become due and payable.

On March 21, 1978, Stephen and Letty Best (Purchasers) contracted to purchase the property, and informed the lender on March 23, 1978, that they would be assuming the loan. The Lender replied on March 29, 1978, that it would consider an assumption, but only if the interest rate were increased from 7½% to 9¼%, the then-prevailing rate; the Lender also stated that the Purchasers would be required to pay one point to the Lender.

The Purchasers refused to increase the interest rate or pay one point, and on May 31, 1979, the Borrowers, without the Lender's approval, conveyed the property by deed to the Purchasers. The deed provided that the conveyance was subject to a note secured by a deed of trust, which the

Purchasers expressly agreed to pay. Subsequently, on July 21, 1978, the Lender notified the Borrowers that "under the terms of the deed of trust the balance is due in full."

On July 3, 1978, the Purchasers filed a bill for declaratory judgment in the Circuit Court of Fairfax County, praying that the court declare that covenant number seven in the deed of trust was null and void; or, alternatively, if such covenant be held valid, that the court declare that consent to conveyance was unreasonably withheld and that the requirement as a condition to approval that the Purchasers agree to increase the interest rate and pay a 1% assumption fee be declared unreasonable.

The Circuit Court of Fairfax County ruled that the Lender had not shown an impairment of security as required under the deed of trust, that the withholding of consent was an unreasonable restraint on alienation, and it ordered that the Lender accept payments from the Purchasers under the existing terms and conditions of the deed of trust. The Lender appealed to the Supreme Court of Virginia.

The Supreme Court of Virginia reversed the judgment of the Circuit Court of Fairfax County, on the basis that the preamble requiring impairment of security conflicted with the unrestricted consent covenant, and therefore, was to be disregarded.

ARGUMENT IN SUPPORT OF ALLOWANCE OF WRIT

INTRODUCTION

The *Best* case arose at a time when so-called "due on sale" clauses were under consideration throughout most

states in the United States, including Virginia. Such clauses are phrased in many ways, but essentially they provide that if the owner of property encumbered by a mortgage or deed of trust undertakes to sell such property, the purchaser may not assume the existing mortgage or deed of trust without the lender's consent. Such instruments generally provide that if there is a sale, the lender has the right to accelerate the indebterness and require full payment, or such lender has the right to modify the interest rate or other terms of the indebtedness. Many courts have held that under such circumstances, a lender has the right to accelerate the indebtedness only if there is impairment of the lender's security; otherwise, the lender's refusal to allow an assumption is an unreasonable restraint on alienation. Other courts have held that the enforcement of such provisions are not an unreasonable restraint on alienation, but may be invoked for other reasons not related to the lender's security. Of course, in recent years mortgage rates have risen dramatically, and the obvious reason for accelerating the loan is so that the lender can loan back the money at much higher rates if such loan is fully paid.

The Supreme Court of Virginia heard such a case, *Lipps* v. *First American Service Corporation*, 223 Va. ....., 286 S.E.2d 215 (1982) in combination with the *Best* case. In *Lipps*, the Court considered a deed of trust entered into after enactment of a code provision, specifically §6.1-330.34 of the CODE OF VIRGINIA, which allows a lender to accelerate an indebtedness if its deed of trust contains specified language which is set out in capitals and clearly authorizes acceleration in the event of a sale. The Supreme Court of Virginia sided with those states which hold that due-on-sale clauses need not be invoked only for reasons of protecting the lender's security.

However, the deed of trust in the *Best* case predated the enactment of §6.1-330.34 and contained language wholly different from the provision required under that

Code Section. It also contained language different from most provisions under consideration in other states, in two very significant aspects.

First, the deed of trust did not state that if the Borrowers convey their property, the Lender has the right to accelerate the loan. It stated that the Borrowers may not convey their property unless the Lender consents to such conveyance.

Secondly, the deed of trust specifically stated that the purpose of the consent clause was to protect the Lender's security; and if the owners violate this consent clause, then the note is automatically accelerated. So what the Lender had done was to take a clause which would otherwise be wholly requgnant to a basic principle of law, to wit, that the owner of property has the right to convey such property, and it has clothed it with conditions that undertake to remove it from the realm of unreasonable restraint and into the realm of legitimate purpose. However, by rejecting the conditions of reasonableness which the Lender attached to its covenant, the Supreme Court of Virginia stripped it back down to what it was on its face: An absolute and unqualified restraint on alienation of title.

In short, the Supreme Court of Virginia could have ruled the same as the Circuit Court of Fairfax County: that the Lender only reserved a right to restrain alienation for reasons specifically tied to the Lender's security, and to invoke its covenant now for another purpose, to wit, to improve its financial position, was unreasonable. Instead, it dismissed the qualifying language and upheld the consent covenant without restriction. What the Lender had awkwardly tried to phrase as a reasonable "due-on-sale" clause the Court had modified into an unconstitutional "restriction-on-sale" clause.

I. The covenant forbidding transfer of title by the owner without the Lender's approval violates the rights of property owners protected by the 14th amendment to the Constitution.

One of the most jealously protected rights of citizens of the United States is the right to own property. An important corollary is the right to dispose of such property. In *Terrace* v. *Thompson*, 263 U.S. 197, 68 L.Ed. 255, 44 S. Ct. 11 (1923), the Supreme Court of the United States stated:

> The 14th amendment, as against the arbitrary and capricious or unjustly discriminatory action of the state, protects the owners in their right to lease and dispose of their land for lawful purposes. . . .

The right to own and dispose of property has heretofore been recognized in the State of Virginia. In *Dunlop* v. *Dunlop's Executors*, 144 Va. 297, 308, 132 S.E. 351 (1926), the Supreme Court of Virginia stated:

> It is unnecessary to go into at length the well-known doctrine that neither a testator in a will not a grantor in a deed can give a fee simple estate in either real or personal property and endeavor to impose upon the donee any condition incompatible with the usual and necessary incidents accompanying a fee simple estate. Among such incidents are the complete right of alienation, without let or hindrance and the liability of the property for the debts of the donee.
>
> . . . it is well settled in this country and in England, from which country we derive the principles of our jurisprudence, that a gift or grant of a beneficial estate, in fee or absolutely, whether legal or equitable, has certain legal incidents of which the estate cannot be divested, and all conditions adopted for that purpose are

necessarily repugnant, and void. Among those incidents are the donee's or grantee's power of alienating such estate, and its liability for his debts . . .

The *Best* case deals with a covenant which prevents the alienation of a fee simple estate by its owner. In rejecting the stated purpose of the preamble as being in conflict with the absolute provisions of the covenant, the Supreme Court of Virginia held, in essence, that the Lender had an unlimited and unrestricted right to forbid transfer of ownership.

Shortly before the *Best* case was argued before the Supreme Court of Virginia, a "due-on-sale" case arising in Virginia was considered by the United States Court of Appeals for the Fourth Circuit, *Williams* v. *First Federal Savings and Loan Association,* 651 F.2d 910 (4th Circuit. 1981). In upholding due-on-sale clauses in general, and refusing to limit their legitimate purpose to protection of the lender's security, the Court nonetheless distinguished the normal due-on-sale case from the clause in the *Best* case. The Court of Appeals stated, at page 925:

. . . Leaving aside, for the moment, the problems associated with changing interest rates, the homeowner may decide to move, preferring another house, or having been transferred by an employer to another part of the country. He wants to sell. *Sometimes ineptly drawn mortgages or deeds of trust make it a breach of contract to sell without the prior consent of the lender. The need to obtain the prior consent of another is a text-book example of an unreasonable restraint on alienation.*

In such a situation, while the due-on-sale clause may not be directly involved, still there is something amiss in the total scheme for dealing with any acceler-

> ation of the otherwise anticipated 30 year obligation. Whenever the thing that is wrong represents an attempted unfair advantage to the lender, the courts, not just in Virginia, but throughout the United States, seek to achieve justice by denying to the usually economically superior lender, which presumably the better bargaining position, other advantages in the package of provisions in the deed of trust concerning acceleration.
>
> . . .
>
> *{This case} . . . involved a flat restraint on alienation* . . . [Emphasis supplied].

As a footnote to the first paragraph above, the Court stated further, also at page 925:

> Even if the only penalty expressed for such a default is the creation of a right to accelerate and to compel repayment in full of the deed of trust note, the imposition in the contemplation of the law in unreasonable. A person should not be placed in a position in which he or she must violate an agreement, must dishonor his promise, to achieve a result.

Stated simply, the Fourth Circuit Court of Appeals distinguished the covenant in *Best* because it is not a "due-on-sale" clause. It is a "restriction-on-sale" clause. It is unfortunate that even after the federal court considered the issue of unreasonable restraint on alienation in the *Best* case, the Supreme Court of Virginia still ignored this issue completely.

A clue to the Court's reasoning in *Best* is found in *Lipps, supra*. There the Supreme Court of Virginia discussed Code §55-59, which governs deeds and trusts, and provides that such deed of trust "shall be construed as given to secure the performance of each of the covenants entered into by the grantor" and also provides for acceleration upon "the

breach of any of the covenants entered into or imposed upon the grantor." The Court said:

> Thus, a general acceleration clause is read into every deed of trust unless otherwise provided in the instrument . . . This acceleration clause covers the breach of any covenant imposed by the instrument on the grantor. This obviously would include a covenant not to convey the secured property without the consent of the lender, 286 S.E.2nd 215, 219.

In effect, the Court ruled that it is not against public policy to require acceleration in the payment of debt upon the violation of any covenant contained in a deed of trust. However, it did not consider whether the covenant itself was against public policy or was in violation of general principles of law.

The logical fallacy in the Court's reasoning arises from its attempt to make the phrase "due-on-sale clause" a term of art when it is not, and to argue from this "universal." This argument runs: "Due-on-sale clauses" are permitted by law. The covenant in *Lipps* is a "due-on-sale clause" and is not an invalid restraint on alienation. The *Best* covenant is a "due-on-sale clause." Therefore, the *Best* covenant is not an invalid restraint on alienation.

However, the fact is that all "due-on-sale clauses" are not automatically valid. For example, a covenant not to convey to a person of the Negro race without the Lender's permission, would be a "due-on-sale clause" under the Court's reasoning. It is obvious that this provision would be an unlawful restraint on alienation, and would be unconstitutional.

Again, it is no answer to say that a racial covenant, is against public policy and unconstitutional. The question

is whether the covenant in *Best*, which absolutely forbids alienation without consent, is against public policy and unconstitutional. In either case, whether it be a racial covenant or a consent covenant, the acceleration clause cannot validate the covenant. The covenant must be separately examined.

The Fourth Circuit in *Williams, supra*, concluded that *Best* involved "a flat restraint on alienation." Indeed, the Court concluded that the covenant was a "text-book example of an unreasonable restraint on alienation." This seems inescapable. The owners agreed they would not convey unless the lender approved, and they could not sell without dishonoring their word, unlike the parties in *Williams*. In comparing the covenant under its consideration with the covenant in *Best*, the Fourth Circuit made precisely the distinction which the Supreme Court of Virginia did not seem to grasp in considering *Lipps* and *Best* together:

> It does not require the lender's consent to a sale. It only permits the lender, at its option, to exercise the due-on-sale clause if there has been a sale, which the Potes, as homeowners, are fully entitled to make without any dishonoring of their word.

651 F.2d at 928.

II. The legal principle adopted by the Court should not have been applied in this case, and led to conclusions which were inescapably unconstitutional.

Rule 5:(42)e of the Rules of the Supreme Court of Virginia provides that the opening brief of appellant shall contain "the principles of law, the argument and the authorities relating to each question presented." Rule 5:43(d)

provides that the brief of appellee shall contain "the principles of law, the argument, and the authorities relating to each question" presented by appellant.

The Court ruled that the obligatory language of covenant 7 conflicted with the preamble which states the purpose of the covenant, and, therefore, the obligatory language must prevail. This principle of law was not presented in the brief of appellants and was never advanced by the Lender in any earlier proceeding, and, therefore, it was not addressed in the brief of appellees and was never argued on their behalf. It came as a complete surprise. The only reference to the preamble in the brief of appellants is printed in the Appendix, *Infra,* at page A-14. There the Lender did not argue that the clauses were in conflict, but that "the clauses in question protect the security of the Deed of Trust by assuring payment of the debt."

So we have the ironic situation where both the Lender and the Borrowers agreed that the two clauses can be read together in harmony, but the Court rejected that stipulation and decided that the covenant is to be interpreted without restriction. If it had ever been advanced by the Lender that the preamble was ineffective and that the Lender had the unresticted right to withhold consent, the Borrowers and Purchasers would have responded that this is unconstitutional.

In reaching its decision, the Court relied primarily on *Scott* v. *Albemarle Horse Show,* 128 Va. 517, 104 S.E. 842 (1920). In that case, the prefatory or recital language of the contract stated that Scott guaranteed to pay for certain improvements on property owned by Albemarle, provided that an option be given to him to purchase the property. The body of the contract provided that Albemarle bound itself to sell the property to Scott and that Scott agreed to take the property at a stated price in accordance with the

terms of the contract. Subsequently Albemarle sued Scott to require him to perform his obligation to purchase the property, and Scott argued that he only had an option to purchase the property, which he could or could not exercise. The trial court held that the obligatory language in the body of the contract was inconsistent with the preamble, and prevailed. The Virginia Supreme Court of Appeals disagreed, and reversed. In its decision, at page 845, it stated:

> *The contract is to be construed as a whole, and effect given to every provision thereof if possible. No word of paragraph can be omitted in construing the contract if it can be retained and a sensible construction given to the contract as a whole.* If, however, there is an inconsistency between the obligatory part of the contract and the recitals therein, the effect will be given to the obligatory part rather than to the recitals, as this is regarded as the more vital and important of the two; but *the recitals are often helpful in the construction of contracts and throw light on the meaning and intent of the parties.* . . . Looking to the obligatory part of the contract, the loan, no obligation to purchase appears to have been given to the appellant, but an option is given to the Horse Show Association to recede from the contract under given conditions and within a given time. The provision in the preamble "that an option is given him to purchase", and, in the contract, that "in consideration of the option to purchase the said property herein mentioned," are apparently inconsistent with the obligatory part of the contract by which the Horse Show Association agreed to sell the property to Scott, and Scott agreed to take the property at the price mentioned in the contract. Hence, according to the ordinary rules of construction, in the absence of explanation, the obligatory part of the contract would be binding and we should be compelled to hold that Scott had agreed to purchase the property, and not merely take an option upon it.

> But it is manifest from the terms of the contract as a whole that it was the intention of the parties to give to Scott an option to purchase the property. [Emphasis supplied.]

So, in the decision cited as primary authority for the decision in *Best*, the Court quoted the general rule that where the preamble conflicts with the obligatory provisions, the obligatory provisions prevail. But the principle does not stop there, and in that case the Court did not invoke that principle. An adjunct to the principle is that a contract must be construed as a whole, and effect must be given to every provision thereof if possible, to determine the intent of the parties. The Court gave meaning and effect to the preamble, even though it conflicted with a subsequent provision.

This principle is restated in *Ames* v. *American National Bank of Portsmouth*, 163 Va. 1, 176 S.E. 204 (1934):

> When two provisions of a contract seemingly conflict, if, without discarding either, they can be harmonized so as to effectuate the intention of the parties as expressed in the contract considered as a whole, this should be done. The presumption always is that the parties have not used words aimlessly and that no provision is merely a superfluity unless it is plainly merely a repetition.

Applying the complete principle of law to the present case, the court should not have discarded the prefatory language, to wit, "in order more fully to protect the security of this deed of trust" in favor of the obligatory language, to wit, "the maker of the note covenants and agrees that he will not assign or transfer the property secured by this deed of trust without approval of the noteholder," if the two provisions could be harmonized so as to effectuate the intention of the parties as expressed in the deed of trust

considered as a whole. The Court did acknowledge that these provisions could be harmonized, as it indicated in its decision that the prefatory language would have been given force and meaning if it had been inserted as a part of covenant 7. The Court was bothered by the fact that the language was contained in the preamble rather than in the covenant itself. However, regardless of where the language appeared, it should not have been summarily dismissed. The clear intention was that the covenant was to be exercised only for the purpose stated in the preamble. This intention must be recognized and enforced, particularly in light of the fact that the deed of trust was drawn by the lender and in case of any ambiguity is to be construed against it.

In *Williams, supra,* the Court commented on the prefatory language contained in the deed of trust in *Best:*

> Sometimes the security instrument may remark that a purpose of the due-on-sale clause is to protect the lender's security. Applying *expressio unius est exclusio alterius,* courts have foreclosed resort to the due-on-sale clause absent a showing by the lender that the security would be impaired.

651 F.2d 927. Applying the entire principle stated in the *Scott* case, *supra,* and the principle stated in *Williams,* the decision in the *Best* case should be: even if the two provisions conflict, the one provision states the purpose for the other, and the two can be harmonized; and if the Lender states one purpose, it cannot invoke the covenant for another, that is, to obtain a higher interest rate.

Although the law regarding interpretation of contracts is to be determined by the individual states, and is not governed by federal law or the Constitution, it is felt it was necessary to review the law to show why a constitutional question has been created because the Court went off on a tangent of its own.

CONCLUSION

It is submitted that in holding that a borrower and lender can lawfully covenant that a borrower cannot transfer its property without the lender's consent, the Supreme Court of Virginia violated the provisions of the Fourteenth Amendment of the United States Constitution. For this reason this Petition for a Writ of Certiorari should be granted.

Respectfully submitted,
GRAYSON P. HANES,

HAZEL, BECKHORN AND HANES
P. O. Box 547
4084 University Drive
Fairfax, Virginia 22030
(703) 273-6644
Counsel for Petitioners and
Counsel of Record

CERTIFICATE OF SERVICE

I hereby certify that three copies of this Petition were delivered to the office of John H. Rust, Counsel for both Respondents, 4069 Chain Bridge Road, Fairfax, Virginia 22030, this 10th day of June, 1982, pursuant to Rule 28, Paragraph 3, of the Rules of the Supreme Court.

s/GRAYSON P. HANES